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Before the
Federal Communications Commission
Washington, D.C. 20554

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| In the Matter of | ) | |
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| Implementation of the Local Competition | ) | CC Docket No. 96-98 |
| Provisions in the Telecommunications Act | ) | |
| of 1996 | ) | |



# BELLSOUTH'S COMMENTS

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## SUMMARY

The Supreme Court has sent the Commission back to the drawing board with some specific instructions on how to approach section 251(d)(2). Those instructions require the Commission to draw from section 251(d)(2) a rational limiting standard on network element unbundling. The Court also instructed the Commission that in applying its limiting standard it *must* look beyond incumbent LEC networks in assessing the availability of present alternatives and the ability of CLECs to create alternatives through self-provisioning. The Court's instructions were informed by the fact that forced sharing may in fact displace competition with regulation rather than the reverse.

The Commission must focus its test on maximizing benefits to consumers. Creating entitlements for competitors to unbundled network elements under the Commission's current TELRIC pricing scheme cannot be the focus of a rational limiting standard on network element unbundling. The Commission could take an important initial step towards this goal by adopting a test it has already applied to network elements as the standard. Thus, the test under section 251(d) should relate to whether an element is necessary to, or whether the failure to unbundle would impair, an efficient CLEC's meaningful opportunity to compete.

The presence of competitive alternatives, the possibility of entry through self-provisioning and whether an efficient CLEC has a meaningful opportunity to compete can only be assessed by looking at properly defined product and geographic markets. The Commission practice when assessing competitive alternatives has been to define markets as the first step in its analysis. This proceeding requires the same approach.

When markets are defined and examined, one inescapable fact emerges -- local conditions vary to the extent that no single one-size-fits-all national list can reflect this variation. Constructing a one-size regulatory straight-jacket would be contrary to the Commission's own attempts to "move away from 'one size fits all' regulation and reduce the regulatory requirements on incumbent carriers as competition develops in discrete geographic areas," *Local Competition Survey* at 4, let alone Congress's pro-competitive de-regulatory goals for the 1996 Act.

The Commission has adopted a three zone approach to aggregating local markets in its *Special Access* and *Switched Transport* orders discussed below. These zones were drawn by the Commission to reflect competition and underlying economic forces that influence competition in local markets. This three zone approach provides one way to develop national lists for local elements that adequately reflect the presence of alternatives to incumbent LEC facilities and the ability of CLECs to self-provision.

CLECs have raised billions of dollars of capital and have invested that capital in alternative facilities. Thousands of miles of local fiber and hundreds of switches have been deployed in the last two years. CLECs have concentrated on using these facilities to serve the business market. The Commission has recognized that competition for larger businesses has been a fact for some time, and that CLEC competition for those customers continues to grow rapidly. Cable telephony presents a rapidly growing direct and complete substitute for residential local exchange servie delivered over incumbent LEC networks. The Commission must account for the role of cable telephony facilities as an alternative to incumbent LEC networks.

The Commission's lists must reflect the market realities set out in great detail below. The facts show that for many incumbent LEC network elements in many geographic areas there are

more than adequate alternatives to incumbent LEC elements. The ease of self-provisioning some elements means that CLECs could create alternatives in sufficiently short order that unbundling would not meet section 251(d)(2)'s standards.

The Commission should simply disclaim any interest in unbundling new network elements that incumbent LEC's are investing in to provide advanced services. Advanced services competition and competitive alternatives come from other networks as well the current ability of CLECs to compete effectively using incumbent local loops and collocation. There are no "incumbents" in this market and there is no incumbent LEC network to unbundle. Because incumbents have just begun deploying the new equipment necessary for them to provide advanced services, any unbundling requirement would unbundle incumbent LEC investment dollars rather than existing equipment. The Commission should be encouraging investment in advanced services equipment, not handicapping it. Any requirement that incumbent LECs invest in new equipment only to turn it over to CLECs once a profit opportunity has been established would create a substantial investment disincentive.

Heeding the Court's advice to develop and apply a rational, limiting unbundling will result in a list that reflects the many alternatives available to CLECs in the market.

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**BELLSOUTH'S COMMENTS**

BellSouth Corporation, on behalf of itself and BellSouth Telecommunications (BellSouth), hereby files these Comments in connection with the Commission's Second FNPRM in CC Docket Nos. 96-98 and 95-185.[1]

## I. INTRODUCTION

The Commission's *First Report and Order* misapplied section 251(d)(2)'s standards for unbundling network elements. The Supreme Court has required the Commission to begin entirely anew.[2] BellSouth's comments set out a framework for implementing the Court's directive that the Commission develop and apply section 251(d)(2)'s necessary and impair standard in a way that creates a rational "limiting standard" on unbundling network elements. In applying this limiting standard, the Commission must look to the availability of competitive alternatives outside incumbent networks and to the ability of competitive local exchange carriers (CLECs) to self-provision network elements. Assessing competitive alternatives for particular

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[1] *In the Matter of Implementation of the Local Competition Provisions in the Telecommunications Act of 1996*, CC Docket Nos. 96-98. *Second Further Notice of Proposed Rulemaking*, FCC 99-70, released April 16, 1999 ("*Second FNPRM*").

[2] *In the Matter of Implementation of the Local Competition Provisions in the Telecommunications Act of 1996*, CC Docket No. 96-98, *First Report and Order*, 11 FCC Rcd 15499 (1996)("*First Report and Order*"), *modified on reconsideration*, 11 FCC Rcd 13042

elements will require the Commission to define product and geographic markets for network elements and to identify all sources of alternative facilities. BellSouth proposes a single approach the Commission can use to assess whether incumbent LEC network elements meet section 251(d)(2)'s standard.

Although a single national standard is appropriate, a single national list of unbundled elements is not. As Commissioner Powell points out in his statement attached to the *Second FNPRM*, the results of applying a national standard to local markets will yield results that depend on local conditions. Providing local exchange service is a local business. The Commission cannot blind itself to the fundamental fact that local competitive and economic conditions vary widely across the country. The Commission's desire for a national list is achievable only if the list reflects the great variation in local conditions. A one-size fits all list would be inherently arbitrary, anti-consumer and contrary to the Court's instructions. Any such list would conflict with the Commission's goal, consistent with the Telecommunications Act of 1996 (Act) and the Court's opinion, "to move away from 'one size fits all' regulation and reduce the regulatory requirements on incumbent carriers as competition develops in discrete geographic areas." *Local Competition Survey* at 4.

The Commission has, in the past, grouped geographic markets based on the competitive similarity of choices available to consumers in each of the markets. BellSouth believes that for elements supplied in local geographic markets, such as loops and transport, the Commission should apply its national standard to the three zone approach it has used to grant incumbent's special access and switched transport pricing flexibility. These zones reflect competition and the

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(1996), *vacated in part, Iowa Utilities Bd v. FCC*, 120 F.2d 753 (8th Cir. 1997), *aff'd in part and rev'd in part sub nom. AT&T Corp. v. Iowa Utilities Board*, 119 S. Ct. 721 (1999).

basic economics that influence construction of competitive facilities. The zones reflect a basic distinction between large cities, smaller urban areas and rural areas. For local market elements, the Commission could easily establish a three zone national list. For elements that are provided in national markets, like operator services and directory assistance, a single national decision is appropriate.

This approach would allow the Commission to develop a workable list of network elements that must be provided at cost-based prices. The list will reflect local conditions for local elements. State commissions would then be free to apply the Commission's national analytic approach to assessing whether peculiar local market features are significant enough to warrant a change in the Commission's list. Based on a thorough fact-based record that reflects local market conditions, a state commission could add to or subtract from the Commission's list.

## II. SUPREME COURT'S OPINION

The Supreme Court singled out two overarching mistakes in the Commission's original approach to unbundling network elements. First, the Commission mistakenly presumed that Congress intended that network elements were to be unbundled wherever technically feasible. This mistaken presumption was the linchpin for the *First Report and Order's* analysis of unbundling. By removing this linchpin, the Court's ruling requires the Commission to start entirely afresh and approach unbundling and the necessary and impair standard with a blank slate. The Court's second lesson is its conclusion that the Commission had failed to draw from the Act's necessary and impair language the rational limiting standard on unbundling that Congress intended. Unbundling without *meaningful* limits is contrary to Congress's basic pro-competitive, deregulatory goal for the Act.

### A. Technical Feasibility and Unbundling

The Court identified a fundamental mistake underlying the Commission's entire original approach to network element unbundling. In the section of its *First Report and Order* addressing unbundling, the Commission began "with the premise that an incumbent was obliged to turn over as much of its network as was 'technically feasible,' and viewed [the statutory necessary and impair language] as merely permitting it to soften that obligation." *Id.* This incorrect premise led the Commission to misinterpret the Act as imposing a general duty on incumbent local exchange carriers (LECs) to unbundle whenever technically feasible. The Court held that the Commission's "premise was wrong." Rather, the Act's "technically feasible" language in section 251(c)(3) relates to "*where* unbundled access must occur, not *which* [network] elements must be unbundled." *Id.* quoting 120 F. 3d, at 810 (emphasis in original).

Correcting this flaw will require the Commission to reverse its presumptions on unbundling and reconsider the basic competitive wisdom of regulatory unbundling. *Iowa Utilities Board*, 119 S. Ct. 736. This will require the Commission to justify unbundling requirements on an element-by-element basis. Doing so will put the Commission back in touch with Congress's pro-competitive intent. Reversing course will also put the Commission on the same pro-competitive wavelength as the antitrust law, and will put it in accord with economic thinking on regulation.

The Act requires the Commission to assess whether network elements should be unbundled on an element-by-element basis. Unbundled access to an element may be required *only* if the element meets section 251(d)(2)'s standard. The Act creates no general presumption in favor of unbundling as the Commission mistakenly concluded. The Court has required the Commission to reverse its mistaken course of presuming that the Act mandates unbundling unless proven otherwise. *Id. Compare First Report and Order,* ¶¶ 281("a determination of

technical feasibility would then create a presumption in favor of requiring an incumbent LEC to provide the element"); 286 ("we conclude that the statute does not require us to interpret the 'impairment' standard in a way that would significantly diminish the obligation imposed by section 251(c)(3)"). Similarly, the Act can not be read to suggest that more unbundling is better than less, as the Commission's original approach seemed to read it. *Iowa Utilities Board*, 119 S. Ct. 754 (Breyer, J.).

Unbundling is permissible only where it furthers Congress's intent, and Congress intended unbundling to occur only when the facts demonstrate that section 251(d)(2)'s necessary and impair standard is satisfied.

### B. The Court's Requirement That "Necessary and Impair" Serve As A Limiting Principle

The Court also held that the meaning the Commission gave to the necessary and impair standard in the *First Report and Order* did not match the terms of the statute or Congress's intent. . The Court explained that "if Congress had wanted to give blanket access to incumbents' networks on a basis as unrestricted as the scheme the Commission has come up with, it would not have included § 251(d)(2) in the statute at all." *Iowa Utilities Board*, 119 S. Ct. at 735. The Court then held that section 251(d)(2) was intended to impose a limiting standard on unbundling, and that the Commission must "apply *some* limiting standard, rationally related to the goals of the Act, which it has simply failed to do." *Id.* at 734-735 (emphasis in original).[3]

The Court singled out two of the Commission's positions on necessary and impair for discussion. Each independently supplied grounds for the Court's holding that the Commission's

[3] The Commission's freedom to consider "other factors" in addition to the necessary and impair tests is discussed below. Whatever "other factors" the Commission may choose to consider, they must be consistent with the Court's instruction that section 251(d)(2) provide a limiting standard.

approach conflicted with the basic thrust of the Act's limits on unbundling. First, the Commission refused to consider the availability of elements outside incumbent networks in assessing whether unbundling was necessary or the failure to unbundle would impair the ability to provide service. The Court held that the "Commission cannot, consistent with the statute, blind itself to the availability of elements outside the incumbent's network." *Id.* at 735. Echoing the antitrust laws, the Court specifically pointed to self-provisioning as an additional source of competitive supply that the Commission must evaluate. *Id.* at 734-735.

Second, the Court held that the Commission's conclusion that *any* increase in cost (or decrease in quality) from failing to unbundle an element of an incumbent's network was sufficient to support an unbundling requirement was contrary to the plain language of the statute. *Id.* at 735. The Commission's approach is "simply not in accord with the ordinary and fair meaning of " necessary and impair. Taking a cost increase (or quality decrease) that simply reduces a new entrant's profits as creating an impairment does not supply the rational limiting standard that the Act requires. *Id.*, n. 11.

## III. DEFINING AN APPROACH TO THE NECESSARY AND IMPAIR STANDARD

The Commission must now articulate a reasoned approach to implementing section 251(d)(2)'s necessary and impair standard that resonates with Congress's pro-competitive deregulatory goals for the Act. As the Court made very clear, the Commission's prior approach did not do so.

### A. The Court's Rules For Necessary and Impair

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Other factors that would expand unbundling beyond that available under the necessary and impair standard would conflict with the Court's opinion and the Act, as discussed below.

The Court has supplied the Commission with guidance on how to properly approach the necessary and impair standard. First, section 251(d)(2)'s necessary and impair standard must supply a limiting principle on network unbundling that is rationally related to the Act's pro-competitive goals. This will require the Commission to give the statute's words -- "necessary" and "impair" -- the weight their "ordinary and fair meaning" requires. *Id.* at 735. "Necessary" and "impair" are strong words. Second, the Commission must look outside incumbent networks when assessing whether unbundling a network element meets the standard. This examination of competitive alternatives must include the ability of carriers to self-provision facilities. Third, the Commission may not order unbundling based on any increase in cost (or decrease in quality). It must articulate some rational standard for assessing the importance of the costs involved. At a minimum, the Commission's approach must include each of these requirements set out by the Court.

### 1. Necessary and Impair Must Supply A Limiting Principle

The Court provided an essential insight by establishing that necessary and impair must supply a limiting standard on unbundling. *Id.* at 734-735. The essential reason for Congress's limiting standard is that the blanket sharing of incumbent networks is fundamentally inconsistent with Congress's "pro-competitive, de-regulatory" Act.

Justice Breyer supplied the reasoning behind the Court's requirement that section 251(d)(2)'s necessary and impair language limit the sharing of elements of incumbent networks.

> Increased sharing by itself does not automatically mean increased competition. It is in the *un*shared, not in the shared, portions of the enterprise that meaningful competition would likely emerge. Rules that force firms to share *every* resource or element of a business would create, not competition, but pervasive regulation, for the regulators, not the marketplace, would set the relevant terms.

*Id.* at 754 (Breyer, J.).[4] Pervasive unbundling, as previously ordered by the Commission, limits the potential for competition and maximizes the need for regulation. Both directly conflict with Congress's basic goal for the Act. "A totally unbundled world ... is a world in which competitors would have little, if anything, to compete about. Such a world is not what the Act envisions." *Id.*[5]

The principal cost of forced unbundling will spring from reduced investment by incumbents and new entrants alike, and therefore reduced real competition.[6] *Id.* at 31 (Breyer, J.). These costs are discussed in more detail below.

Justice Breyer also spelled out that unbundling carries with it "significant" administrative costs. *Id.* at 753. These costs increase as the complexity of the elements and their importance to the incumbent firm increase. *Id.* at 753-754. One reason for this is the need for increasingly complex administrative proceedings to set the terms and conditions for sharing.[7] For example,

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[4] The unbundled network element platform nicely illustrates Justice Breyer's point. As envisioned by at least some CLECs, the platform would have the incumbent supply all the elements for CLECs to provide service in a single bundle. This bundle would be provided at TELRIC prices without CLEC investment or risk. This platform would reduce or eliminate the need for CLECs to build competitive facilities, and thus reduce competition. Although it provides for some form of retail arbitrage, this arbitrage hinders competition by sacrificing normal, unregulated market incentives to invest in competitive facilities. The platform is sharing every resource and leads to exactly Justice Breyer's result -- pervasive regulation substituting for competition. The platform and other combinations are discussed in more detail below.

[5] The *Jorde, Sidak and Teece* affidavit, discussed in more detail below, expands upon Justice Breyer's thinking. As Justice Breyer explained, a sharing requirement reduces incentives to invest. The affidavit spells out just how serious a reduction in investment by both incumbent ILECs and CLECs can occur. Mandatory unbundling is not itself a route to competition.

[6] The Commission's TELRIC pricing methodology maximizes the disincentives from cost-based unbundling by minimizing the potential for obtaining market-based rewards for investment.

[7] One example of how administrative complexity rapidly increases is the requirement that local switching be unbundled. Although the Commission may view this requirement as creating a single required element offering, in fact it has spawned many. BellSouth's price lists include 8 different unbundled switch port offerings. Each much be separately priced and administered. BellSouth's unbundled element price list includes 61 primary offerings. The regulatory literature does not support the notion regulators can set prices in such detail across such a broad range of technologically complex products and services without harming consumer welfare. The

BellSouth's unbundled network element price list contains 18 densely packed pages of prices. These regulatory proceedings create the delay and uncertainty that the Commission hopes to avoid. *Second FNPRM* at ¶ 13. A rational limiting principle will account for both the competitive and administrative costs of unbundling and the unnecessary delay and dependence on regulatory proceedings that it occasions.

> Regulatory rules that go too far, expanding the definition of what must be shared beyond that which is essential to that which merely proves advantageous to a single competitor, risk costs that, in terms of the Act's objectives, may make the game not worth the candle.

119 S.Ct. 754 (Breyer, J.).

These cautions against pervasive unbundling underlie Congress's choice of "necessary" and "impair" as the measures of its standard. Both are strong words that were intended to create a high threshold that parties must satisfy to claim an entitlement to unbundled elements. They must be interpreted and applied consistent with the Court's requirement that section 251(d)(2) supply a limiting standard. Congress created less restrictive standards for mandating incumbent LEC actions where it judged them, *e.g.* broad interconnection and resale requirements. Congress's desire for "rapid deployment" of advanced services provides another illustration of a standard not inserted into section 251(d)(2).

Congress's sharp distinction between resale and unbundling obligations, and the establishment of a high standard for unbundling, reflects a reasoned decision based on the economic realities set out by Justice Breyer that mandatory unbundling at prices set by regulators has substantial, concrete costs that can easily outweigh any supposed consumer welfare benefits. The Court's opinion makes it clear that Congress's procompetitive, deregulatory plan requires

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rapid pace of change in the industry, both technological and in corporate alliances, magnifies the potential harm of the Commission's previous central-planning approach.

that section 251(d)(2) be applied to create opportunities for competition rather than opportunities for regulation.

### 2. The Commission Must Look Outside Incumbent Networks To Alternative Facilities And Self-Provisioning

The Commission's original approach to the necessary and impair standards concluded that the availability of network elements outside incumbent networks was irrelevant to the need for a sharing requirement. The Court rejected this and required the Commission to weigh the ability of new entrants to self-provision an element or purchase access to it from a provider other than the incumbent LEC. *Id.* at 735. In doing so, the Court discussed and dismissed the Commission's underlying reasoning that "'requiring new entrants to duplicate unnecessarily even a part of the incumbent's network'" justified imposing an unbundling requirement. *Id.* quoting *First Report and Order*, ¶283.

The Court's message is that having new entrants duplicate incumbent networks is to be sought rather than avoided. Certainly the Commission's prior approach of requiring unbundling at cost-based prices in order to minimize CLEC investment in local facilities makes little policy sense. Investment in local facilities by CLECs and incumbents benefits consumers. By providing CLECs risk-free access to elements at TELRIC prices, the Commission's policy provides a substantial disincentive to CLEC investment in facilities.

Limiting unbundling so that free-riding does not interfere with normal incentives to invest in competitive facilities is a fundamental goal of section 251(d)(2)'s limiting principle and should be a fundamental goal of the Commission. Where competitive facilities can coexist with incumbent facilities, the Commission should not be providing incentives to CLECs to depend on

regulation rather than their own investment.[8] Simply put, the Commission may not justify an unbundling requirement because it saves CLECs from constructing network facilities. Sacrificing competition in the unshared portions of the network for sharing would contravene the Act and the Court's opinion.

### 3. Any Increase In Cost Must Be Substantial To Meet The Necessary And Impair Standard

The Court explicitly rejected the notion that any increase in cost justifies a sharing requirement. *Id.* The Court found that an increase in cost from obtaining an alternative to an incumbent element that only reduces a CLECs profit could not justify an unbundling requirement. Any cost increase must be material enough to have some ultimate effects on consumers, as discussed below.

The Court's analogy was that as long as the light bulb could still be changed, the incumbent's longer ladder was neither necessary nor would its absence impair the CLEC. By encouraging CLECs to substitute an incumbent's ladder when their own could be made to work, the Commission tipped the balance away from CLECs investing in their own facilities, and the resulting competition in the unshared facilities, to pervasive regulation of the shared facilities. The Court's opinion requires the Commission to base an unbundling requirement only on meaningful cost increases.

Comparing the costs of CLEC facilities to incumbent facilities must be done on an apples-to-apples basis. TELRIC prices set under the Commission's rules cannot be the standard

[8] Following through on the Court's mandate to look outside incumbent LECs' networks will give the Commission information on where, and what type of, CLEC facilities are currently operating and what capabilities CLECs have for self-provisioning. For example, during the three years since passage of the Act, CLECs have installed many switches and miles of transport. Commission examination of CLEC build-out plans would doubtless magnify this trend and remove any factual basis for unbundling of advanced services, transport and switching elements.

for comparison. For example, a CLEC claim that the costs of its own element so substantially exceeds the costs of an incumbent element priced at TELRIC that it cannot offer service is not probative of anything. TELRIC is a hypothetical price and does not reflect the incumbent's actual costs. As long as the CLEC seeks to compare its actual cost to something, that something must be the incumbent's actual cost. The Court did not appear interested in comparing hypothetical ladders.

## IV. SOURCES OF PRACTICAL GUIDANCE FOR DEVELOPING A FRAMEWORK FOR APPLYING THE NECESSARY AND IMPAIR STANDARD

The Commission need not reinvent the wheel to develop a framework for applying the necessary and impair standards in a way that meets the Act's requirements. Although the necessary standard creates a higher hurdle, the analytical approach outline below applies to both. There is a large body of precedent at the Commission and developed under the antitrust laws that addresses how to implement Congress's procompetitive goal for the Act. Whether under the necessary or the impair standard, the ultimate goal of creating entitlements to network elements at cost-based prices is to maximize competition and the consumer welfare benefits competition creates. *See generally*, 3A P. Areeda and H. Hovenkamp, *Antitrust Law*, ¶¶ 771-77 (1996); *Hausman and Sidak Affidavit*, ¶¶ 45-47 attached to USTA Comments filed in this proceeding. (*Hausman and Sidak Affidavit*). Creating benefits for particular competitors alone will not benefit competition or consumers, and thus can never meet Congress's procompetitive goals for the Act.

Commission and antitrust precedent set out below outline a clear and well-established approach to evaluating competitive alternatives and the ability of firms to self-provision, as required by the Act and the Court. These precedents create a logical process for assessing

competitive alternatives and competition. The process requires that markets be defined, competitors identified and the possibility for new entry and expansion be assessed. The final assessment of competition also requires examination of alternative avenues to compete for end user customers.

### A. Defining Product And Geographic Markets

Competition occurs within markets and it is only within properly defined markets that the competitive effects of business and policy choices can be evaluated. Providing local exchange and exchange access is fundamentally a *local* business, and the network elements used to provide local service are often tied to these local markets. In order to determine whether unbundling a network element would benefit competition and consumers, the Commission must understand local market conditions. Antitrust analysis of essential facility claims is always performed within a defined market.[9] This can only be done within the context of properly defined economic markets.[10]

The Commission has adopted the market definition principles set out in the *Merger Guidelines*. *LEC Regulatory Treatment Order* at 15773-15774. The *Merger Guidelines* require that both a product market and a geographic market be defined. Product markets are defined by assessing whether a hypothetical monopolist of a particular product or service could profitably raise price above competitive levels. If enough consumers would shift to an alternative product

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[9] *See, e.g., Blue Cross & Blue Shield United of Wisconsin v. Marshfield Clinic*, 65 F.3d 1406-10 (7th Cir. 1995); 3A P. Areeda & H. Hovenkamp, *Antitrust Law*, ¶ 773 (1996).

[10] *See, e.g., In the Matter of Regulatory Treatment of LEC Provision of Interexchange Services Originating in the LEC's Local Exchange Area and Policy and Rules Concerning the Interstate, Interexchange Marketplace*, CC Docket Nos. 96-149 and 96-61, *Second Report and Order in CC Docket No. 96-149 and Third Report and Order in CC Docket No. 96-61*, 12 FCC Rcd 15756 (1997) (LEC Regulatory Treatment Order) at 15800 ("a relevant geographic market must be defined in order to conduct an accurate assessment of market power").

or service to make the price increase unprofitable, the alternative must be included in the market, and the analytic process repeated. *Id.* at 15775-6, 15782 (demand-side considerations determine product market definition).

Geographic markets are defined similarly by assessing whether a hypothetical monopolist in a narrow geographic area could profitably raise prices above competitive levels. If enough consumers would shift to suppliers in other areas to make the price increase unprofitable, the alternative areas must be included in the geographic market, and the analytic process repeated. *Id.*

The Commission must place each network element it is evaluating in a defined product and geographic market. It is only within properly defined markets that competitive alternatives to a particular network element, or any other competitive asset, can be assessed. Geographic markets for some elements like loops and transport are likely to be local. However, geographic markets for other elements -- operator services and directory assistance as examples -- are likely to be national.

Some network element markets are likely to be provided on an essentially point-to-point basis.[11] The Commission has established criteria for grouping individual point-to-point markets into larger geographic markets. Where consumers in a larger area face "the same competitive alternatives for a product," that entire area can be treated as a single geographic market. *Bell Atlantic/NYNEX* Order at 20016-7. Thus, the Commission has used LATAs and MSAs as geographic markets for local exchange and exchange access. *Id.* at 20017-8. The Commission

[11] *In the Application of NYNEX Corporation, as transferor, and Bell Atlantic Corporation, as Transferee, For Consent to Transfer Control of NYNEX Corporation and Its Subsidiaries*, File No. NSD-L-96-10, *Memorandum Opinion and Order*, 12 FCC Rcd 19985, 20016-7 (1997) (*Bell Atlantic/NYNEX Order*).

may similarly group point-to-point-type network elements and other elements delivered in local geographic markets.

In the sections below, dealing with individual network elements, BellSouth suggests appropriate product and geographic market definition and market groupings.

### B. Identifying Market Participants And Their Significance

Once a market for a particular network element is defined, the Commission can identify the competitors in that market and the competitive alternatives available to the network element under consideration. Competitors include all those currently producing or selling in the market. *Merger Guidelines* § 1.31. This includes the output of vertically integrated firms, *id.*, and firms that have committed to enter the market. *Id.* at n. 27. Firms or facilities not currently in the market but which could enter within a year without the expenditure of significant sunk costs are counted as current market participants.[12] *Id.* The Commission has recognized the importance of supply substitution responses. *LEC Regulatory Treatment Order* at 15782, n. 121 ("supply substitutability identifies all productive capacity that can be used to produce a particular good, whether it is currently being used to produce that good or to produce some other, even unrelated, good"); *AT&T Reclassification Order,* 11 FCC Rcd 3271, 3303-05.

In assessing competitive alternatives, self-provisioning or ease of entry may trump any seeming limits on competitive alternatives. *Merger Guidelines* § 3; *Areeda & Turner.* The government's expert competition agencies have set a two year time horizon for assessing the competitive benefits of entry. *Merger Guidelines* § 3.2. The judgment is that entry within two

[12] This may be particularly relevant to the consideration of competition in switching. The evidence indicates that switches may be installed in well under a year. Switch capacity already in the market may be substantially expanded in that time. Wireless and long distance may be converted at least partially to local use within a year through software upgrades. Sunk costs vary among these different routes, but may not be "substantial" under any of them.

years is timely enough to prevent consumer harm, and that governmental intervention in that market would not produce consumer benefits. Although the Commission may not be bound by this two year time horizon for assessing competitive alternatives, it would do well to adopt the same pro-competitive judgment as the expert competition agencies.

### C. Assessing Competition

In assessing competitive alternatives to incumbent network elements and the consumer effects of forced unbundling, the Commission has already established a number of useful guideposts. The Commission has recognized that end user markets, "where a final product or service is sold to end-user customers," are distinct from input markets, "where the product or service is sold to firms that use it as an input in producing other products or services."[13] Network elements are inputs that are used to produce telecommunications services. As antitrust analysis makes clear, a "monopoly" of an input may not create any monopoly power to raise prices to end users. Thus, the essential facilities doctrine requires that the firm controlling the essential facility be a monopolist of some end user service. *MCI Communications v. AT&T Corp.*, 708 F.2d 1081, 1132-33 (7th Cir. 1982), *cert. denied*, 464 U.S. 891 (1983). Similarly, an input patent may carry with it no power to raise prices if there are alternative ways to reach end users.[14]

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[13] *In re Application of Teleport Communications Group, Inc., Transferor, and AT&T Corp., Transferee, for Consent to Transfer Control of Corporation's Holding Point-to-Point Microwave Licenses and Authorizations to Provide International Facilities-Based and Resold Communications Services*, CC Docket No. 98-24, *Memorandum Opinion and Order*, 13 FCC Rcd 15236, 15245 (1998) (*AT&T/Teleport Order*).

[14] "Although the intellectual property right confers the power to exclude with respect to the *specific* product, process, or work in question, there will often be sufficient actual or potential close substitutes for such product, process, or work to prevent the exercise of market power." *1995 Department of Justice and Federal Trade Commission Antitrust Guidelines for the Licensing of Intellectual Property* § 2.2. A natural gas pipeline may be the only gas pipeline to a particular customer, but if that customer is a large industrial firm it can substitute among natural gas, coal or other energy sources or justify extension of a competing gas pipeline to its facilities.

The Commission must carefully consider the impact of unbundling what may seem on the surface to be "essential" input facilities where there are alternative routes to compete for end users. For example, in many locations local exchange service or advanced services can be delivered to consumers over cable or wireless facilities. Where the local telephone loop no longer provides the potential to determine consumer prices, subjecting the local telephone loop to unbundling at cost-based prices would serve no pro-competitive or pro-consumer purpose. 3A P. Areeda & H. Hovenkamp, *Antitrust Law* ¶ 773.

A final Commission competition finding is of general applicability here. The Commission's orders defining local service markets have recognized that demand for local service can be separated into distinct markets based on demand characteristics. In the *Bell Atlantic/NYNEX Order*, the Commission found that residential and small business customers, medium-sized businesses and large businesses/government users were sufficiently distinct to require separate examination. *Bell Atlantic/NYNEX Order* at 20016 ("[b]undles of services that appeal strongly to one segment ... are often not acceptable substitutes for the services preferred by the other segments). More recently the Commission has determined that the three categories could be combined into two: mass market and larger businesses. *AT&T/Teleport Order* at 15247. However, it may be on closer examination that a three-part division more accurately reflects market dynamics.

The different demands exhibited by these different groups has given rise to varying levels of service competition and varying levels of competitively supplied alternatives to incumbent network elements. The Commission has found that entry into the larger business market is

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*Hartigan v. Panhandle E. Pipe Line Co.*, 730 F. Supp. 826, 866 (C.D. Ill. 1990), *affirmed, State of Illinois v. Panhandle E. Pipe Line Co.*, 933 F.2d 1469 (7th Cir. 1991).

relatively easier than into the mass market, and that numerous new entrants are rapidly entering the larger business market. *Id.* at 15250.

## V. A BALANCED APPROACH TO APPLYING SECTION 251(d)(2)'s STANDARD TO NETWORK ELEMENTS

This section provides an approach to further defining and applying the Act's unbundling standard to network elements. The suggested approach is informed by traditional competitive analysis, consumer welfare principles and the Act's essential pro-competitive, deregulatory goals.

As an initial matter, and before applying section 251(d)(2)'s standard, the Commission should determine whether unbundling the network element in question is technically feasible. If unbundling is not technically feasible, it cannot be required.[15]

### A. The Necessary Standard

Section 251(d)(2)(A) requires the Commission to consider whether unbundling of proprietary network elements is "necessary" to offer a service. Consistent with the high degree of legal protection normally accorded intellectual property, the Act requires consideration of whether a proprietary element is "necessary."

The necessary standard should apply to what is traditionally thought of as intellectual property. The Department of Justice Intellectual Property Guidelines treat as intellectual property work subject to patent, copyright, trade secret or similar protections. *See* U.S. Department of Justice and Federal Trade Commission, *Antitrust Guidelines for the Licensing of Intellectual Property* Section 1 (1996). A network element is proprietary if it contains

[15] The essential facilities doctrine contains a similar limitation. *See MCI Communications Corp. v. AT&T Co.*, 708 F.2d. 1081, 1132-33 (7th Cir. 1982), *cert. denied*, 464 U.S. 891 (1983)(essential facilities plaintiff must show "the feasibility of providing the facility").

"proprietary protocols or elements containing proprietary information." *First Report and* Order at 15641-2.

Intellectual property is subject to extensive protection under patent law, statute and common law because preserving incentives to invest in the creation of intellectual property creates large social benefits. The Department of Justice's broad definition of intellectual property is tailored with a view towards maximizing the consumer benefits of competition and minimizing regulation. As such, it is in harmony with Congress' goals for the Act and should be adopted by the Commission.

Forced sharing of intellectual property at cost-based prices is antithetical to the well-recognized consumer benefits of investing in the development of intellectual property.[16] A patent, for example, grants to the patent holder a right of exclusive use of his or her invention. 35 U.S.C. §§ 101, 154, 161, 171 (1994). This right includes the right not to use or license a patent. *Id.* Patent and other intellectual property laws protect the rights of inventors to maximize the profits from their labor and risk-taking. *Kewanee Oil Co. v. Bicron Corp.*, 416 U.S. 470, 480-81, 484 (1974).

To ensure that forced sharing of intellectual property is necessary, the burden of proof must be placed on parties seeking access. These parties should be required to demonstrate that the benefits of forced access to the intellectual property at issue at cost-based prices clearly outweighs the costs. Forced sharing promises significant social costs in reduced investment as inventors are denied the benefits of their labor and competitors are free to reduce investment in certain areas knowing that they can ride on the incumbents innovation at cost. *See Jorde, Sidak*

[16] "[A] sharing requirement may diminish the original owner's incentive to keep up or to improve the property by depriving the owner of the fruits of value-creating investment, research, or labor." *Iowa Utilities Board*, 119 S.Ct. 753 (Breyer, J.).

*and Teece Affidavit* attached to USTA Comments filed in this proceeding (*Jorde, Sidak and Teece Affidavit*).

Consistent with the Commission's past competitive practices and the antitrust laws, the only cognizable benefits to be weighed in this analysis are benefits to consumers. The fact that a CLEC could profit from cost-based access to an incumbent LEC's intellectual property cannot alone justify a sharing obligation. The patent and antitrust laws both protect the right to exclusive use of intellectual property laws in order to ensure that innovators have an opportunity to reap a reward for the risk they have undertaken.[17]

The Commission must avoid any definition or application of the necessary standard that would create a perception that incumbent LEC investment in innovation would be freely available to all at cost-based prices.[18] Doing otherwise would risk dampening incentives to create innovative offerings. The Commission should take two steps to accomplish this. First, since CLECs, incumbent LECs and other firms are equally free to invest in innovative advanced or enhanced local offerings, and various competitive outlets for such innovations now exist, there is no reason to require forced sharing of innovative intellectual property in these areas.[19] Second, the Commission should require parties seeking cost-based sharing of intellectual property to demonstrate that the intellectual property at issue is necessary to provide basic local exchange or exchange access service. This would limit forced sharing to those intellectual property inputs that are necessary to basic service and the development of local competition as it

[17] U.S. Department of Justice and Federal Trade Commission, *Antitrust Guidelines for the Licensing of Intellectual Property* Section 1 (1996).

[18] This reduction in investment, and consequent consumer harm, from cost-based unbundling mandates must be considered before unbundling is ordered. BellSouth suggests that this is best done explicitly, as set out below.

[19] The Department of Justice recognizes that markets for innovation are generally highly competitive.

was understood at the time the Act was passed. Innovation aimed at new and advanced services should be free from the investment damper created by the prospect of forced sharing. The Commission should clearly state that no such sharing will be compelled in order to maintain market incentives provided by the intellectual property and antitrust laws to invest in innovation.

The Commission's application of section 252's pricing rules to shared intellectual property should not destroy the social benefits of investment in innovation and intellectual property.

### B. The Impair Standard

Section 251(d)(2)(B) contains a second standard that requires the Commission to consider whether failure to unbundle any network element would impair the ability of a requesting carrier to offer telecommunications service. In developing and applying a test, the Commission must identify a goal that is consistent with Congress' pro-competitive, deregulatory intent. As outlined earlier, the right goal is maximizing consumer welfare. Assessing impairment against a consumer welfare standard allows the Commission to ensure that its standard and the application of that standard is aimed at protecting competition, not competitors. The steps to properly developing and applying a test are set out below.

#### 1. Defining The Impair Standard

"Impair" should require an important or material reduction in an efficient CLEC's meaningful opportunity to compete. In the *First Report and Order*, the Commission used a phrase that provides the proper context for applying "impair" in the context of unbundling. Section 251(c)(3) requires that incumbent LECs provide "any requesting carrier" access to unbundled elements in a "just [and] reasonable" manner. The Commission interpreted this to mean that network elements must be provided in a way that "would provide an efficient

competitor with a meaningful opportunity to compete."[20] *First Report and Order* at 15660. By using an "efficient competitor" as the standard, the Commission properly focused the test on competition instead of particular competitors. The Commission also avoided the quagmire of a CLEC-by-CLEC opportunity test that would have set an incumbent's provisioning requirements by the ability or inability of each CLEC to manage its own business.

The Commission's test also properly stressed that the measure is "meaningful opportunity" to compete rather than some guarantee of competitive success. This test well serves consumer welfare and Congress' pro-competitive deregulatory goals by providing efficient competitors the opportunity to compete, and then letting the market decide success or failure.

If failing to unbundle a network element takes away an "efficient" competitor's "meaningful opportunity to compete," the impairment standard is properly met because competition and consumer welfare may well suffer.[21] As noted above, the Commission has already used this standard to determining *how* network elements must be provided. The standard fits equally well for defining *which* elements must be unbundled. This standard also meets the Court's requirement that the Commission assess competitive alternatives and the relative costs of those alternatives. These are best measured by determining if an efficient competitor has a meaningful competitive opportunity to compete without those facilities.

Assessing whether a meaningful opportunity to compete has been impaired requires a point of comparison, a norm or baseline situation against which to measure. AT&T presents one

[20] No objection to this interpretation has been lodged at the Commission or with the courts.

[21] The reduction in investment, and consequent consumer harm, from cost-based unbundling mandates must also be considered before unbundling is ordered. BellSouth suggests that this is best done as proposed below.

extreme at which the baseline could be located. *AT&T Ex Parte*, Docket No. 96-98 "Remand Proceeding on Rule 319" at 37. In essence, AT&T argues that the baseline should be a universal, instant, problem-free rollout of the broadest possible line of local service at maximum convenience to the CLEC. *AT&T Ex Parte* at 11. If failing to unbundle a network element would have a negative effect measured against that benchmark, AT&T would have the Commission declare the impair standard met and require unbundling at cost-based prices. (For whatever reason, the prospect of unbundling the other wireline network into the home draws from AT&T a radically different answer. Apparently, AT&T believes that no degree of impairment of the breadth, timing or convenience of competitors rolling out competitive advanced services over the cable network could even begin to justify an unbundling requirement.)

Of course, AT&T's suggested benchmark is ludicrous. It certainly violates the Court's requirement of a rational, limiting standard and the goal of the Court's requiring the Commission to decide whether unbundling meets the requirements of section 251(d)(2) rather than essentially delegating that decision to CLECs. *Iowa Utilities Board*, 119 S.Ct. 736. Creating some other worldly CLEC utopia where work, risk and investment are reduced to a minimum by entitlements to incumbent network elements was not Congress' goal.

Congress specified that impairment results from the inability to offer service, *not* the inability to roll out service in a way that no business ever has. The proper standard against which to measure impairment is a realistic business plan for service rollout that would create competitive benefits for consumers. BellSouth has substantial experience rolling out service, whether it involves enhancements to its wireline network or construction from the ground-up of

new cellular, PCS networks and networks in foreign countries. No business plan for creating a new service offering is built on universal, instant, problem-free rollout of the broadest possible line of local service at maximum convenience.

### 2. Applying The Impair Standard

Determining whether the lack of access to a particular element would impair an efficient CLEC's meaningful opportunity to compete requires a fact-based analysis of competitive alternatives and the possibility of entry or self-provisioning. As noted above, the Commission must also analyze end user competition to determine if unbundling would create competition that benefits consumers or that just benefits particular firms. Mandatory unbundling at cost-based prices will always create potentially lucrative possibilities for arbitrage, especially given the historical end user pricing of local service. The Commission's goal should be to determine that impairment relates to "meaningful opportunities to compete" instead of to opportunities to profit from arbitrage that creates no real consumer benefits.

The Commission and the antitrust agencies analyze competition by defining markets, identifying the competitors and the competitive facilities in the market and then assessing entry possibilities. Then the competitive situation can be meaningfully assessed. *Bell Atlantic/NYNEX Order* at ¶ 37; *LEC Regulatory Treatment Order*, 12 FCC Rcd 15756; *Merger Guidelines*. The Commission should follow those same steps in applying the impair standard. That analysis will require facts on competitive facilities and competitive options, including installation of new facilities and expansion of old, and the costs and benefits to CLECs from investing in alternative facilities. Facts about alternatives routes to competition for end users must be gathered to assess the potential consumer benefits or harms from unbundling.

## C. Other Factors

Section 251(d)(3) allows the Commission to "consider" other factors. Fidelity to Congress's intent and basic rules of statutory construction require that any other factors that the Commission considers be consistent with those Congress wrote into this section and the "limiting" standard on unbundling that the Court held Congress intended.

Congress's inclusion of the phrase "at a minimum" in Section 251(d)(2) indicates that the Commission may establish principles for unbundling that go beyond the necessary and impair standards. But because "agency discretion . . . does not encompass the authority to contravene statutory commands," any additional factors that the Commission considers may not override the necessary and impair tests expressly set forth in Section 251(d)(2).[22]

Specifically, the Commission permissibly might determine that a network element should not be subject to mandatory unbundling even if it passes the necessary and impair standards. Such a determination might be based on a judgment that requiring cost-based unbundling would, on balance harm consumer welfare due to the disincentives it creates to investment, or simply because of the administrative burden it may create. But the Commission may not require unbundling of an element that fails the necessary or impair tests. Otherwise – if the Commission could use additional factors to trump the necessary and impair tests – it could nullify the Supreme Court's command that the Commission must "giv[e] some substance to the 'necessary' and 'impair' requirements." AT&T Corp. v. Iowa Utils. Bd., 119 S. Ct. 721, 736 (1999). Indeed, the Supreme Court made clear that the statutory necessary and impair tests are "standard[s] [that

[22] Farmworker Justice Fund, Inc. v. Brock, 811 F.2d 613, 622 (D.C. Cir. 1987); see also Robbins v. Reagan, 780 F.2d 37, 48 (D.C. Cir. 1985) (per curiam) (Congress intends agencies to make decisions "based on factors solely related to the goal of implementing the stated statutory purposes in a reasonable fashion, rather than taking irrelevant or impermissible factors into account").

must] be[] met," not simply considerations that might be relevant to the Commission's analysis. See 119 S. Ct. at 735.

Reducing the statutory tests to subordinate "considerations" also would violate the dictate that the Commission should "tak[e] into account the objectives of Act" when applying Section 252(d)(2). Id. at 736. Section 251(d)(2) implements Congress's judgment that efficient, facilities-based entry is the key to local telecommunications competition.[23] To encourage that competition, Congress placed a "limitation upon network-element availability." 119 S. Ct. at 734. Congress designed the 1996 Act to maximize incentives for investment and the welfare of consumers, not the profits of competitors. Thus, Congress did not want new entrants to have a mandatory right of access to the incumbent's network when they are able to compete without such access. Any attempt to evade this statutory limitation, and thereby extend regulation to areas where Congress wanted unfettered competition, would slow or stop the deployment of new facilities by incumbents and CLECs alike.

The social costs of creating a CLEC entitlement to incumbent LEC assets at cost-based prices set by regulators must be considered in the Commission's analysis. Otherwise, no reasoned judgment on the consumer welfare effects of forced unbundling could be made. Although this essential analytical factor could be considered within the necessary and impair

[23] See, e.g., AT&T Corp. v. Iowa Utils. Bd., 119 S. Ct. at 753 (Breyer, J., concurring in part, dissenting in part) ("[t]he unbundling requirement seeks to facilitate the introduction of competition where practical, i.e., without inordinate waste"); S. Conf. Rep. No. 104-230, at 1 (1996) (Act "designed to accelerate rapidly private sector deployment of advanced telecommunications and information technologies"); id. at 148 (drafters contemplated that Act would promote facilities-based, "local residential competition"); Notice of Proposed Rulemaking, Order on Remand, and Waiver Order, Amendment of the Comm'n's Rules to Establish Competitive Serv. Safeguards for Local Exchange Carrier Provision of Commercial Mobile Radio Servs., 11 FCC Rcd 16639, 16678-79, ¶ 80 (1996) ("[t]he interconnection provisions of the Act, Section 251 and 252, are designed to promote facilities-based local exchange competition").

analysis, the Commission and consumers would be best served by making it a third, explicit factor.

The substance of this third factor is to require the introduction of facts concerning, and explicit analysis of how, unbundling and access under whatever the Commission's then-current pricing standard is likely to affect CLEC investment in competitive facilities and incumbent LEC investment in new and improved facilities. This factor should be a necessary component of any evaluation of mandatory unbundling because forcing unbundling at cost-based prices has substantial and far-reaching affects on competition and consumers.

Unbundling an incumbent LEC network element and requiring its provision at cost-based prices creates disincentives to CLEC investment in competing facilities. *Jorde, Sidak and Teece Affidavit* at ¶¶ 47-54; *Hausman and Sidak Affidavit* at ¶¶ 78, 86-88. Potential access to unbundled incumbent facilities at cost-based price introduces a new element into any CLEC's investment decision. Access to those elements "substantially decreases a CLEC's incentives to make a sunk investment." *Jorde, Sidak and Teece Affidavit* at ¶ 47. Where risky investments are involved, unbundling "tips the balance of the CLEC's calculus in favor of waiting" because the CLEC can simply wait until the ILEC makes the investment to see if the investment will succeed. The CLEC can then use the incumbent asset at a cost-based price. *Id.* at ¶ 49.

Mandatory unbundling at cost-based prices will obviously reduce incumbent LECs' investment incentives. Justice Breyer explained that "[n]or can one guarantee that firms will undertake the investment necessary to produce complex technological innovations knowing that any competitive benefits deriving from those innovations will be dissipated by the sharing requirement." *Iowa Utilities Board*, 119 S. Ct. at 753 (Breyer, J.).

> Regulatory use of cost-based rates (such as TELRIC) creates negative economic incentives for new investment and for innovation in telecommunications. If the new investment succeeds, the CLEC can purchase the ILEC's unbundled element at cost, as set by TELRIC. If the new investment does not succeed, the CLEC competitor does not bear any of the cost.... If the cost-based rate of the unbundled elements corresponding to the new service were set exactly at the cost of providing the new service, with no return to R&D costs and no reward to uncertainty, then regulation would completely eliminate the economic incentive to provide the new service, because the expected return to the ILEC would *always* be negative.

*Hausman and Sidak Affidavit* at ¶¶ 75, 77 (footnotes omitted, emphasis in the original).

The results of analyzing this factor may lead the Commission to refrain from unbundling particular elements that it might otherwise have ordered unbundled. Such a result would be consistent with consumer welfare and the Court's insistence that Congress intended a limiting standard rather than an expansive one.

### D. The Burden Of Proof

Unbundling is not always, or even usually likely to increase consumer welfare. *Jorde, Sidak and Teece Affidavit.* Mandatory unbundling, particularly at cost-based prices, will always have social costs, by reducing investment and imposing administrative costs on society. It may have social benefits (and will have, if done properly) in a narrower set of circumstances. As Justice Breyer explained in his opinion in *Iowa Utilities Board*, competition will occur in the *un*shared parts of the network, not in the shared parts. The social costs of unbundling suggest that the burden of proof be placed on the parties seeking unbundling.

Section 251(d)(2) contemplates placing the burden of proof on the same parties. It requires a positive demonstration that a network element is necessary or that failure to unbundle it would impair before unbundling the element can be justified.

Finally, the burden of proof should also be placed on CLECs because the information is most directly in their hands and they may have little incentive otherwise to produce it. BellSouth does not have direct access to internal CLEC information and the Commission has not gathered the information from CLECs that would support a conclusion that any network element meets section 251(d)(2)'s standard for unbundling.[24]

### E. The Role Of The State Commissions

The Commission can and should articulate a single national approach to defining a section 251(d)(2) test and a methodology for applying it. The Commission can and should determine a list of unbundled network elements that reflects the diversity in local conditions. As described in detail below, BellSouth believes that local markets can be grouped into three zones. The Commission's national list of these local markets would simply distinguish unbundling obligations among the zones, as required by market facts.

State commissions, applying the Commission's national test and methodology, would then play two important roles where they could bring their knowledge of local market conditions to bear. First, carefully applying the Commission's standards for applying section 251(d)(2), they could modify the Commission's three-zone national list where local market peculiarities require. This would be limited to adding or removing network elements previously identified by the Commission from the list of unbundled elements in a particular zone. As discussed above, the burden of proof must ultimately be borne by the party seeking entitlement to an element

[24] *Local Competition Survey* at 1, 6("[t]he voluntary surveys do not provide comprehensive information about the number of switched lines CLECs provide to their customers solely over their own facilities. This is the missing piece of information that is required"). Even as to unbundling local loops, the Commission cannot simply assume that unbundling meets the statutory standard given the dynamism inherent in today's market. Cable telephony, fixed wireless loops and cellular and PCS offerings require, at a minimum, careful consideration as alternatives to the local telephony loop.

under section 251(d)(2).[25] The party would have to show that the local market is substantially different from other markets in its geographic grouping and that the element met the Commission's section 251(d)(2) standard. Given the rapid pace at which CLECs are deploying competitive facilities, the Commission should mirror market realities and establish a strong presumption against modifying its list through additions of elements it has not included on its list of unbundled elements While reducing the list is consistent with Congress's de-regulatory goals, adding to it is not. A party seeking to add an element should be required to demonstrate by clear and convincing evidence that section 251(d)(2) is satisfied.

Second, state commissions would consider CLEC requests for creating new network elements -- that is, requests for elements that have not previously been defined as such by this Commission. Such requests will fall into two categories, only one of which should be open to consideration. Requests in the other category should be precluded by Commission rule.

Some requests will be for elements that are present in incumbent LEC networks, but which CLECs have not sought to unbundle yet. As set out above, given the rapid pace at which CLECs are deploying competitive facilities and Congress's de-regulatory intent, requests for new elements should be required to demonstrate by a clear and convincing margin that the new element meets section 251(d)(2)'s requirements.

The Commission should adopt a rule precluding the unbundling of elements that are new to incumbent LEC networks. Such elements can be deployed effectively by CLECs. The investment disincentives created by the possibility of unbundling new investment are very substantial.

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[25] The ultimate burden of proof must remain on the party seeking entitlement to unbundled element even where removing an element is at issue. However, when an incumbent seeks to remove an element from the list, it should bear the initial burden of going forward.